State Investment Commission
Monthly Meeting Minutes
Wednesday, May 22, 2013
9:00 a.m.
Room 135, State House

The Monthly Meeting of the State Investment Commission (SIC) was called to order at 9:03 a.m., Wednesday, May 22, 2013 in Room 135, State House.

I. Roll Call of Members

The following members were present: Mr. J. Michael Costello, Mr. Thomas Fay, Mr. Robert Giudici, Ms. Paula McNamara, Ms. Marcia Reback, Mr. Andrew Reilly, Mr. Frank Karpinski, and General Treasurer Gina Raimondo. Also in attendance: Mr. Darren Lopes and Mr. Larry Brown of TIAA-CREF; Mr. Thomas Lynch and Mr. Steve Nesbitt of Cliffwater, alternative investment consultant to the Commission; Mr. John Burns of Pension Consulting Alliance (PCA), general consultant; Ms. Sally Dowling, of Adler Pollock, legal counsel; Ms. Anne-Marie Fink, chief investment officer and members of the Treasurer's staff; Mr. James Alvarez from the office of Governor Lincoln Chafee and various local reporters. Ms. Rosemary Booth-Gallogly was absent.

Treasurer Raimondo called the meeting to order at 9:03 a.m.

II. Approval of Minutes

On a motion by Mr. Giudici and seconded by Ms. Reback, it was unanimously

VOTED: To approve the draft of the minutes of the April 24, 2013 meeting of the State Investment Commission.

II. Defined Contribution Plan Quarterly Update

Mr. Lopes reviewed the total portfolio. He said there are currently $85 million in assets through March. He briefly reviewed the number of meetings TIAA-CREF has had with participants through the end of March. He said TIAA-CREF is trying to increase the number of contacts made with participants. He added that the unions have said they will support the outreach efforts once mediation is over.

Ms. Fink added that they are working on rolling out online informational outreach when teachers are back from summer break.

Mr. Fay asked what percentage of the total participants have made contact with TIAA-CREF.

Mr. Lopes said about 26% of the participants have contacted TIAA –CREF by website, telephone or face-to-face meetings.

Mr. Brown reviewed the performance of the plan to date.

III. Real Estate Secondary Sale Update

Ms. Fink said she is working with buyers and trying to determine the best combination of assets to provide the maximum return. A couple of assets are getting more deeply discounted, so they have been dropped from the process. She estimates in 30 to 45 days the process will be complete.

IV. Risk Review

Mr. Burns reviewed the evolution of the ERSRI asset allocation. He reiterated the goal was to reduce volatility without reducing expected return. He said this goal was accomplished by reducing risk through diversifying assets. He reviewed the allocation and level of volatility for 2008, 2010 and 2012. He noted the allocation to equity has been lowered to 38% from 62.5% and that alone has lowered risk.

Ms. Fink went on to talk about how the portfolio measures its risk with standard deviation. She explained how volatility affects the compound return. She said even if the expected return was the same, when the long-term effect of volatility is factored in, there is higher return over time from lower volatility. She said the focus is on building a robust portfolio that will perform well in any kind of environment.

Mr. Nesbitt reviewed the current allocation to hedge funds. He noted hedge funds were selected to achieve better risk-adjusted performance. He said the ERSRI portfolio returned over 12% compounded on an annual basis with about 6% volatility since adding hedge funds. He gave a brief update on hedge fund performance through the end of April. He said the hedge funds are the portfolio's asset class with the best risk-adjusted return.

Ms. Fink added that the hedge fund allocation was purposely designed to be the low risk element of the portfolio. Hedge funds were selected for that characteristic.

Mr. Nesbitt went on to explain the selection of the number of hedge funds Cliffwater recommended. He said Cliffwater recommends typically recommends fewer hedge funds than the rest of the industry. He said at 13 to 15 hedge funds, the majority of diversification benefits have been captured. He went on to explain the performance valuation process for the hedge funds. He briefly reviewed Cliffwater's operations due diligence when selecting hedge funds and how it thoroughly vets managers' processes as well as their valuation procedures.

Mr. Lynch added the vast majority of assets that hedge fund managers invest in are listed securities with readily available prices. He also said each hedge fund manager has a third-party entity that does the valuation; therefore, independence and listed securities give a high level of confidence.

Ms. Reback expressed concern over the independence of the third parties doing the valuation.

Ms. Fink said they have a high level of confidence in these third parties because they don't depend on only one client and they are large brand name corporations who are concerned about their reputations.

Mr. Nesbitt further explained the process behind Cliffwater's operations due diligence and the process of selecting independent auditors.

Mr. Costello asked how many hedge funds had not made the cut from all hedge funds available.

Mr. Nesbitt explained there are about 7,000 hedge funds. He explained Cliffwater tracks about 2,000 of those and then considers about 500-600 of those to meet the institutional fiduciary standards the SIC would require.

Ms. Reback asked if Cliffwater received any compensation directly or indirectly from any hedge fund.

Mr. Nesbitt said that they did not.

Ms. Reback asked why they reported to the SEC that they did.

Mr. Nesbitt explained that they report to SEC that they may receive compensation from insurance companies that have an ownership interest in money manager firms. He said they have never received any compensation from any hedge fund.

Mr. Nesbitt went on to review benchmarks for hedge funds. He explained three of the most commonly used indices: the HFRI Fund Weighted Index, the HFRI Fund of Funds Index and the

Dow Jones Credit Suisse Index. He said Cliffwater uses the Fund of Funds index. He said the Fund of Funds Index is the most commonly used among institutional clients because these funds are professionally managed funds.

VI. Legal Counsel Report

There was no legal update.

VII. CIO Report

Ms. Fink reviewed the portfolio's performance for the last month and reviewed each asset class.
She said PCA is now engaged to review the investment lineup for the CollegeBound Fund.
Ms. Fink said the banking transition has gone smoothly and is now complete.
She said the change in the OPEB account allocation is complete and over time staff will look into more closely mirroring the pension plan asset allocation. She added there are some challenges given the size of the assets and legacy issues.
Mr. Fay asked if the OPEB process was done all at once and what date.
Ms. Fink said it was done over time and it was done in mid-April.
She gave a brief update on the infrastructure RFP. Staff met with four of the managers last month and are starting to do reference checks and continuing the process.
Ms. Fink added that the process is ongoing with corporate governance.
She gave a brief look at current month performance. She added the asset allocation and the diversification are continuing to pay off.
Ms. Reback voiced her concern over why a comparison of performance fees between last fiscal year and four years ago cannot be done.
Ms. Fink said that because private equity incentive fees are not billed but rather collected from gain on sales. GASB does not require tracking them. She said those particular fees were not tracked under the prior administration but are being tracked now. She also said the fees for fiscal year 2012 have been released and will continue to be monitored and reported.

VIII. Treasurer Report

Treasurer Raimondo gave an update on the investor relations portal. She said that as of this morning more information have been added to the portal. She said asset allocation and fees paid by each fund for fiscal year 2012 have been added.
Ms. Reback suggested that the value of the assets should also be added to the portal.
Treasurer Raimondo reassured the board that currently ERSRI is among the most transparent public pension fund in the country and will continue to work towards it.
Ms. Fink added that only five other state pension funds release any information about performance fees.
Mr. Reilly expressed concern over how the transparency of the portal may impair negotiations in the future and the board should be mindful of that.
Treasurer Raimondo added that it will be something that has to continually be balanced.
She thanked the board for their collective work.

There being no other business to come before the Board, on a motion by Ms. Reback and seconded by Ms. McNamara, the meeting adjourned at 10:57 a.m.

Respectfully submitted,

Gina M. Raimondo
General Treasurer